No. 76-1487

In the Supreme Court of the United States

OCTOBER TERM, 1977

CONTINENTAL CASUALTY COMPANY,
Petitioner,

v.

CHAMPION INTERNATIONAL CORPORATION

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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Champion's Opposition attempts to characterize this case as a garden-variety application by the court of appeals of settled New York law to particular facts, and as one that therefore does not warrant further consideration (Opp. at 18). In fact, the Petition for Certiorari presents significant legal questions which raise fundamental constitutional issues concerning the sources of the law to be applied by lower federal courts in the exercise of their diversity jurisdiction. Resolution of these questions is required first to eliminate the unfortunate uncertainty that this case now creates in insurance law, and second to eliminate a potentially substantial burden on interstate commerce in products liability insurance.

1. In diversity cases, questions concerning the proper construction of contracts of insurance are governed by

the entire body of substantive law expounded by the courts of the appropriate state. *Ruhlin* v. *New York Life Insurance Co.*, 304 U.S. 202, 205 (1938); *see Miree* v. *DeKalb County*, No. 76-607, decided June 21, 1977, slip op. at 3. Despite Champion's attempt, by quotation of part of a sentence from the lower court's decision (Opp. at 3-4, 19), to create the misimpression that it applied the law of New York, the face of the opinion clearly demonstrates that the Second Circuit did *not* apply State law but, instead, interpreted the language of the contract according to its own, necessarily federal principles of construction.

The threshold question facing the Second Circuit was whether the language of the policy—specifically the term "occurrence"—could be construed on its face. Under well-established principles of federal law governing diversity cases, this in itself is a question to be decided under New York law. The New York Court of Appeals has unambiguously held that such operative words defining the number of separate "events" entitled to insurance coverage are terms of art whose meaning cannot be facially determined but must be resolved in accordance with an underlying theory of causation.

The Second Circuit deviated from the rule of *Erie R.R.* v. *Tompkins*, 304 U.S. 64 (1938), when it erroneously interpreted the term "occurrence" in accordance with its own, or federal, construction of the contract, instead of applying well-established New York law. The New York cases authoritatively hold that separate "events" of injury constitute multiple "occurrences" for insurance purposes when, as here, the instances of damage are remote in time and space from one another and no one incident of damage caused another. *See Arthur A. Johnson Corp.* v. *Indemnity Insurance Co.*, 7 N.Y.2d 222, 196 N.Y.S.2d 678, 683, 164 N.E.2d 704 (1959); *Hartford Accident & Indemnity Co.* v. *Wesolowski*, 33

N.Y.2d 169, 350 N.Y.S.2d 895, 305 N.E.2d 907 (1973); *Sturges Mfg. Co.* v. *Utica Mutual Life Ins. Co.*, 37 N.Y.2d 69, 371 N.Y.S.2d 444, 332 N.E.2d 319 (1975). If the Second Circuit had looked to and followed New York substantive law, as required by *Erie*, it would have reversed the district court.[1]

2. Moreover, the Second Circuit's decision has created a square conflict among the courts of appeals. *See Maurice Pincoffs Co.* v. *St. Paul Fire & Marine Ins. Co.*, 447 F.2d 204 (5th Cir. 1971); *Hamilton Die Cast, Inc.* v. *United States Fidelity & Guaranty Co.*, 508 F.2d 417, 420 (7th Cir. 1975). The conflict does not, as Champion suggests (Opp. at 6, 22, 25-26), concern the propriety of inconsistent results stemming from a "permissible difference" in state court rules which, under *Erie*, the federal courts must apply in diversity cases. Rather, the conflict concerns whether federal diversity courts must look to State law for the substantive definition of the term "occurrence" in insurance policies or whether the Constitution grants federal courts the power to formulate an independent body of contract law. Champion has not challenged our assertion that the Fifth and Seventh Circuits have unambiguously held that federal courts must apply State law in defining this term.

The uncertainty in the source of commercial law to be applied in diversity cases created by the Second Circuit's decision warrants immediate clarification. The court of appeals' decision threatens to unsettle the parties' expectations concerning the law which will govern insurance

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[1] Champion nevertheless argues that the court of appeals reached the same result as the New York courts would have reached. Champion's assertion is premised on a collection of New York cases reciting general canons of construction to be used in interpreting insurance policies (Opp. at 19-20). The general canons cited by Champion are irrelevant to the issues in this case, however, because the New York Court of Appeals has already rendered precise holdings on the point of law that frustrates Champion's claim.

contracts covering a large portion of the nation's insurance commerce and thus may impose a substantial burden on interstate commerce. The practical problems created by the decision below therefore are of sufficient significance to warrant the grant of certiorari.

Two terms ago, this Court considered a similar diversity case, in which the court of appeals refused to apply the conflict of law rule of the State which created the underlying cause of action, but instead formulated and applied its own principle. *Day & Zimmermann, Inc.* v. *Challoner*, 423 U.S. 3 (1975). In a *per curiam* opinion, the Court granted certiorari, vacated the judgment below and remanded the case with instructions that the court of appeals identify and follow the conflict rule of the appropriate State. *Id.* at 4-5. In light of the explicit decision of the Second Circuit not to apply New York law on the threshold legal question presented to it but to adopt its own rules of interpretation, a disposition like that in *Challoner* would be equally appropriate here. Therefore, we respectfully submit that the judgment of the court of appeals should be vacated and the case remanded for determination and application of New York law.

3. The court of appeals' refusal to follow New York law also leaves open the question whether its departure from *Erie* could be justified because application of State law would have imposed an unconstitutional burden on interstate commerce.[2] The New York cases themselves contain extensive discussions of the three different theories of causation applied by various states in deter-

[2] In apparent reliance on the doctrine of *Lawn* v. *United States*, 355 U.S. 339, 362 n.16 (1958), Champion suggests that this argument cannot be considered in this Court because the argument was not raised below. However, this question entered the case for the first time only after the court of appeals refused to apply New York law. Therefore, the jurisprudential principle stated in *Lawn* is inapplicable here, because the issue could not have been raised at any earlier stage of this litigation.

mining the number of separate "events" covered by insurance policies. *See, e.g., Arthur A. Johnson Corp.* v. *Indemnity Insurance Co., supra.* And it has long been established that the Commerce Clause imposes restrictions on the States' selection of substantive laws in fields normally reserved to their discretion. *See* Horowitz, *The Commerce Clause as a Limitation on State Choice-of-Law Doctrine*, 84 Harv. L. Rev. 806 (1971); *cf. Bibb* v. *Navajo Freight Lines, Inc.*, 359 U.S. 520 (1959). This case presents an appropriate vehicle for consideration of whether the Commerce Clause acts as an independent constitutional constraint upon federal courts' obligations under *Erie* to apply State law in diversity cases.[3]

[3] Champion also suggests (Opp. at 4, 14) that this case does not warrant further consideration because the prevalent uncertainty as to the meaning of the term "occurrence" is a product of faulty draftsmanship which the insurance industry itself may someday alleviate. However, as noted in the Petition (Pet. at 11 n.8), the ambiguity cannot be eliminated by redrafting the definition of the "event" which gives rise to a right of compensation. The inconsistency in interpretation persists because several States adhere to different and incompatible theories of causation. Thus, the same conflict of authority has emerged after each industry attempt to rewrite the operative terms of its policies. *See Elston-Richards Storage Co.* v. *Indemnity Insurance Co.*, 194 F. Supp. 673 (W.D. Mich. 1960), *aff'd*, 251 F.2d 627 (6th Cir. 1961), and *Union Carbide Corp.* v. *Travelers Indemnity Co.*, 399 F. Supp. 12 (W.D. Pa. 1975); *compare* the partial history of the drafting of the current definition at Opp. 13-14 n.8 *with Maurice Pincoffs Co.* v. *St. Paul Fire & Marine Ins. Co., supra.* In any event, the Petition does not seek this Court's interpretation of a contractual provision but instead seeks resolution of the source of the law to which a federal diversity court should look in interpreting such language.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be granted.

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